South Carolina Department of Insurance

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MARK SANFORD
Governor

SCOTT H. RICHARDSON
Director of Insurance

Via Hand Delivery

December 16, 2009

The Honorable Glenn F. McConnell
President *Pro Tempore*
South Carolina Senate
101 Gressette Building
Columbia, South Carolina 29201

The Honorable Robert W. Harrell, Jr.
Speaker
South Carolina House of Representatives
506 Blatt Building
Columbia, South Carolina 29201

Re: Report of the Workers' Compensation Advisory Committee

Dear Senator McConnell and Speaker Harrell,

At the request of the Workers' Compensation Advisory Committee, I am enclosing for your review a report of the Committee's recommendations for improvements in the State's workers' compensation laws. This report is in follow up to the Committee's March 24, 2009 report.

As you may recall, the Department of Insurance has been charged with providing administrative support for the Workers' Compensation Advisory Committee, created pursuant to South Carolina Code of Laws § 42-3-120. As the Department's legislative liaison, the Committee has requested that I provide you with a copy of the enclosed report. I have also enclosed a listing of the Governor's appointees to the Committee for your reference.

Should I be of additional assistance on this matter, please do not hesitate to call me at 803.737.6124 (office) or 803.429.7796 (cell).

Sincerely,

Kendall Buchanan

Kendall R. Buchanan, Legislative Liaison

Enclosures

Cc: Chairman David Thomas, Senate Banking and Insurance Committee
Chairman William E. Sandifer III, House Labor, Commerce and Industry Committee
Governor Mark Sanford c/o Jeff Schilz, Policy Director
William E. Shaughnessy, Chairman, Workers' Compensation Advisory Committee

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Workers' Compensation Laws of South Carolina: A Report on Compliance Issues

Workers' Compensation Advisory Committee
c/o South Carolina Department of Insurance
1201 Main Street, Suite 1000
Columbia, South Carolina 29201

December 16, 2009

TURNER PADGET
TURNER PADGET GRAHAM & LANEY P.A.

CHARLESTON
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MYRTLE BEACH

December 16, 2009

William E. Shaughnessy
Email: WShaughnessy@TurnerPadget.com
Writer's Direct Dial: (864) 552-4602

RE: Governor's Advisory Committee Report Calendar years 2008 & 2009

Dear Members of the General Assembly:

It is a pleasure to forward to you the 2008 – 2009 recommendations of the Governor's Advisory Committee.

The Committee is concerned over the rapid increase in premium costs in the state of South Carolina and the competitive disadvantage this creates in our state's ability to attract new industry or foster new investment by existing industry.

It is the unanimous consensus of the Advisory Committee that an effective way to lower the cost of workers' compensation insurance in South Carolina is to bring more employers into compliance with the South Carolina Workers' Compensation Act.

Many employers evade their legal responsibility to purchase workers' compensation coverage or misclassify employees to create a premium shortfall. When an insufficient amount of premium is collected to pay claims, rate increases on compliant employers result. Further, those employers who refrain from purchasing compensation coverage or who misclassify their employees, enjoy a competitive advantage over their competitors (contractors who cheat on workers' compensation costs may underbid competitors who are paying fair market rates for workers' compensation insurance.

Much of the problem exists in the construction industry. South Carolina is no different from many other states which have noticed problems within the construction industry and have promulgated legislation in an attempt to rectify those problems.

Should any further information or explanation be necessary, kindly feel free to call.

BUSINESS • LITIGATION • SOLUTIONS

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With best regards, I remain

Very truly yours,

TURNER PADGET GRAHAM & LANEY P.A.

William E. Shaughnessy, Esq.
Chairman, Advisory Committee for the
Improvement of Workers' Compensation Laws

WES/ksm
Enclosure

cc: Millie Williams (via email)
William L. Smith, II (via email)
James E. Sanderson, Jr. (via email)
John F. Seibert (via email)
Kendall Buchanan (via email)

WORKERS' COMPENSATION COMPLIANCE ISSUES IN SOUTH CAROLINA

An effective way to lower the cost of workers' compensation insurance in South Carolina is to bring more employers into compliance with the South Carolina Workers' Compensation Act. Employers who are evading their responsibility to purchase workers' compensation coverage or who are misclassifying employees create a premium shortfall. An insufficient amount of premium is collected to pay claims, which triggers rate increases and creates inequities among subcontractors. Some contractors who cheat on workers' compensation costs may underbid competitors who are paying fair market rates for workers' compensation insurance. Furthermore, the South Carolina Workers' Compensation Uninsured Employer's Fund is an expensive drain on tax revenues that could be put to better use, particularly in this time of fiscal austerity. In fiscal year 2007-2008, the UEF paid out over 9.5 million dollars (collection actions by the UEF recouped only a small percentage of the overall expenditures).

1. **Problem Area**: Compliance within the construction industry. A significant percentage of uninsured claims occur within the construction industry. Higher tier and general contractors are often uninsured. Frequently, they allege that they have no employees or do not have the requisite number of employees to make them subject to the Act, because they operate mostly through subcontractors. The factual scenario is the reverse – they often have dozens of employees. The employees of their subcontractors are their statutory employees, but they are able to evade their insurance responsibilities under the Act because their work structure is not immediately visible. The payment of cash wages and off the book schemes, as well as a deliberate misclassification is of epidemic proportions in South Carolina, as well as other states.

Possible Solution: Expand the statutory definition of employee within the construction industry.

What a statutory section might look like:

When used in this Title, unless the context clearly requires otherwise, the following term shall have the following meaning:

1. "Construction industry" means for profit activities involving any building, clearing, filling, excavation, or substantial improvement in the size, use, or appearance of any structure or the appearance of any land. However, "construction" does not mean a homeowner's act of construction or the result of a construction upon his or her own premises, provided the owner is not in the "construction industry" and such premises are not intended to be sold, resold, or leased by the owner within one (1) year after the commencement of construction.
2. "Employee" includes any person who is an officer of a Corporation and who performs services for remuneration for such corporation within this state, whether or not such services are continuous. Any officer of a Corporation may elect to be exempt, as per the provisions of §42-1-520 and a corresponding regulation of the South Carolina Workers' Compensation Commission.
3. "Employee" includes:
    (a) A sole proprietor, partner, or member of a limited liability company who is not engaged in the construction industry, devotes full time to the proprietorship, partnership, or limited liability company, and elects to be included in the definitions of employee by counting himself under his own policy.

(b) An independent contractor, sole proprietor, partner or member of a limited liability company that is engaged in the construction industry. An employee so designated may elect to insure himself under his own policy, in addition to his employee, if any. However, an employee so designated may, if he obtains a workers' compensation policy for his employees, elect to be exempt from the policy by presenting a certificate of exemption issued by the South Carolina Workers' Compensation Commission. The certificate of exemption serves only to exempt the certificate holder from the Act, not his employees, if any. The process for completing an application for a certificate of exemption is described further in this chapter.

4. "Employee" does not include a sole proprietor, partner, member of a limited liability company, or independent contractor not working or performing services in the construction industry. In order to meet the definition of independent contractor not engaged in the construction industry, at least four of the following criteria must be met:

(a) The independent contractor maintains a separate business with his or her own work facility, truck equipment, materials, or similar accommodations:

(b) The independent contactors holds or has applied for a federal employer identification number, unless the independent contractor is a sole proprietor who is not required to obtain a federal employer identification number under state or federal regulations;

(c) The independent contractor receives compensation for services rendered or work performed and such compensation is paid to a business rather than to an individual;

(d) The independent contractor holds one or more bank accounts in the name of the business entity for purposes of paying business expenses or other expenses related to services rendered or work performed for compensation;

(e) The independent contractor performs work or is able to perform work for any entity in addition to or besides the employer at his or her own election without the necessity of completing an employment application or process; or,

(f) The independent contractor receives compensation for work or services rendered on a competitive-bid basis or completion of a task or set of tasks as defined by a contractual agreement, unless such contractual agreement expressly states that an employment relationship exists.

2. **Problem Area**: When the South Carolina Uninsured Employers' Fund handles cases on behalf of employers who have failed to secure workers' compensation policies, in violation of the South Carolina Workers' Compensation Act, the South Carolina Uninsured Workers' Compensation Fund is given rights to obtain reimbursement of money expended to pay workers' compensation awards. In those actions by the South Carolina Uninsured Employers' Fund against employers who have not secured compensation, the employer often will assert that the Fund overpaid the claim or negligently handled the defense of the employee's claim, thereby

killing any effort which could be made by the South Carolina Workers' Compensation Uninsured Employer's Fund to expeditiously conclude that claim.

Possible Solution: Make it impossible for an employer, in violation of the Act, to defend a claim by the South Carolina Workers' Compensation Uninsured Employer's Fund to recoup costs by alleging the claim was mishandled, negligently handled, or overpaid by the South Carolina Workers' Compensation Uninsured Employers' Fund.

What the section might look like:

§42-7-200(h):

Any employer which fails to acquire necessary coverage as required by this Section shall not be allowed to defend claims of the South Carolina Workers' Compensation Uninsured Employers' Fund to recoup costs, expenses, and benefits paid by asserting the defense that the Fund mishandled or negligently handled the defense of their employees' claim or that the Fund overpaid the employee in settling the claim.

3. **Problem Area**: There are some exceptions but the general rule of thumb that employers that regularly have four or more employees must be insured. The governing statute is: "§42-1-360, which states in pertinent part:

> This Title does not apply to:
>
> 2. any person who has regularly employed in service less than four employees in the same business within the state or who had a total annual payroll during the previous calendar year of less than $3,000.00 regardless of the persons employed during that period;

Employers in the construction industry often evade their workers' compensation liability by purporting they have no employees and use only subcontractors.

A review of the workers' compensation threshold requirement in the states establishes:

(a) Thirty-five states don't allow numerical exceptions, such as we have in South Carolina. The other states, to include South Carolina, have threshold requirements that vary from one to five employees, and one state, Texas, does not mandate workers' compensation coverage except for state employees.

Possible Solution:

Classifying independent contractors in the construction industry as employees would go a long way toward identifying employers as being in non-compliance that are presently able to evade the Act by misclassifying their employees as independent contractors.

Although not reflected in the proposed statutory section hereinbelow, perhaps the legislature may want to reverse the $3,000.00 threshold.

What a statutory section might look like:

1. Amend §42-1-360 to read as follows in pertinent part:

This Title does not apply to:

(2) any person not engaged in the construction industry who has regularly employed in service less than four employees in the same business within the state or who has a total annual payroll of less than $3,000.00, regardless of the number of persons employed during that period.

4. **Problem Area**: Some of the most complex litigation before the Commission involves the issue of whether a worker is an independent contactor or employee.

Possible Solution: Exclude workers from the Act that present the most problematic cases.

What a statutory section might look like:

"Employee" does not include:

(a) Bands, orchestras, and musical and theatrical performers, including disc jockey, if a written contract evidencing an independent contractor relationship is entered into before the commencement of such entertainment or service;

(b) A volunteer, unless there is substantial evidence that a valuable consideration was intended by both employer and employee. Consideration does not include customary mileage and per diem;

(c) An exercise rider who does not work for a single horse farm or breeder and who is compensated for riding on a case-by-case basis, provided a written contract is entered into prior to the commencement of such activity which evidences that an employer/employee relationship does not exist;

(d) A person who performs services as a sports official for an entity sponsoring an inter-scholastic sports event or for a public entity or private, non profit organization that sponsor an amateur sports event. For purposes of this paragraph, such person is an independent contractor. For purposes of this subparagraph, the term "sports official" means any person who is a neutral participant in a sports event, including, but not limited to, umpires, referees, judges, lines persons, score keepers, or time keepers. This sub paragraph does not apply to any person employed by a school district, school board, or like person, who serves as a sports official as required by the employing school board or who serves as a sports official as part of his or her responsibilities during normal school hours;

(e) A professional athlete, such as professional boxers, wrestlers, baseball, football, basketball, hockey, polo, tennis, and similar players, and motor sports teams competing in a motor racing event;

(f) A domestic worker hired in a private home to perform general household services, such as babysitting, cooking, cleaning, laundering, gardening, yard and maintenance work. However, this worker if employed by an employer that has contracted with a private home to provide domestic services, is a covered employee of the domestic employer;

(g) A home-care worker hired in a private home to provide primary care to an individual, such as assistance walking, bathing, supervising the use of medications, and administering exercise therapy. However, this worker, if employed by an employer that has contracted with a private home to provide home-care services, is a covered employee of the home-care employer;

5. **Problem Area:** The overwhelming majority of cab drivers in South Carolina are uninsured; however, they are in most instances clearly employees because of the element of control. Cases of cab drivers that have come before the Commission are always convoluted. Cab companies go to great lengths to make their drivers independent contractors, to include creating shell companies that lease independent drivers to an operational company. A South Carolina Supreme Court case that is often quoted in cab cases the Yellow Cab case. Cab companies often design their companies and contractors around the exceptions in that case.

Possible Solution: Correct the problem of non-compliance at the source. Since cab companies must be licensed in most jurisdictions in South Carolina, require that they must provide a certificate of workers' compensation insurance coverage before a license is issued.

What a statutory section might look like:

Notwithstanding provisions of Title 58 regarding a person that is otherwise not exempt under §42-1-360, that provides a taxicab, limousine or other passenger vehicle for hire to the general public, a governing body in South Carolina that issues and renews licenses of taxi and limousine services shall require a certificate of workers' compensation insurance as a condition for obtaining or renewal of a license. There is the presumption that the driver of a vehicle is a covered employee.

6. **Problem Area**: §42-1-380 and §42-1-390 are the source of significant confusion because the statutory language is complex and the enforcement protocols they outline are cumbersome or unworkable. Also, the Commission's corresponding supplemental regulations to the Sections – Regulation 67-403 (election to adopt the Act) and Regulation 67-404 (withdrawing from the Act) - probably cause more problems than they solve. For example, Regulation 67-404 requires an otherwise exempt employer – an employer that does not regularly have four or more employees, but at some time in the past purchased insurance – to file a Form 38 to come out from under the Act. Unfortunately, few employers have ever heard of a Form 38. This requirement ultimately causes considerable problems when uninsured employers genuinely believe they are exempt from the Act because they maintain a work force of less than four employees. Because, however, they failed to file a Form 38 with the Commission, they, as well as the taxpayers of South Carolina, become liable for compensable uninsured claims. Some employers finding themselves in this predicament have been financially devastated, because the

South Carolina Workers' Compensation Uninsured Employers' Fund stepped into their shoes to pay their uninsured claims, and then, afterward, prosecuted a collection action against them. Having a regulatory provision that catches employers by surprise which may serve a purpose of ultimately providing coverage for an uninsured claim, is in reality cheap law enforcement. A good faith argument can be made that the provision is not in accordance with the law because it is contrary to the stated statutory provision of exempting employers that do not regularly have four or more employees.

The two statutory sections, § 42-1-380 and §42-1-390, currently read as follows:

§42-1-380 – Waiver of exemption by employer:

> Any person employing employees in the state and exempted from the mandatory provisions of this Title may come in under the terms of this Title and receive the benefits and be subject to the liabilities of this Title by filing with the Commission a written notice of his desire to be subject to the terms and provisions of this Title. Any such person shall come under the provisions of this Title and be affected thereby thirty days after the date of such notice.

§42-1-390 – Withdrawal of waiver of exemption by employer:

> Any employer who, having elected to come under this Title, being at the time exempt from this Title, and subsequently desiring to withdraw under its terms, may give notice in writing either to the Commission that he no longer is under the terms of this Title or to his insurer who shall give notice in writing to the Commission that the employer is no longer under the terms of this Title. If the insurer does not give notice to the

Commission as required by this Section, the insurer must pay a penalty of $1,000.00 to the Commission which shall be used by the Commission to offset the cost of administering the provisions of Title 42. In the case where the employer gives notice to the Commission that he is no longer under the terms of this Title, the Commission shall in turn, within thirty days of the receipt of the employer's notice, inform the employer, in writing, that he must provide written notification by a date certain to his employees of his withdrawal from the terms of this Title; however, no employer is required to so notify his employees unless the Commission informs him he must do so, as required by this Section. At the expiration of sixty days from the date of the written notice to the Commission, the employer no longer is liable under the terms of this Title and may be permitted to set up any defense as he may be advised to any action brought against him for personal injury or death by accident to an employee.

Possible Solution: Amend the above Sections to simplify the statutory language and remove the elements from the Sections which have been the most problematic.

What amended statutory provisions might look like: Amend §42-1-380 and § 42-1-390 to read as follows:

§42-1-380 – Waiver of exemption by employer:

Any person employing employees in the state and exempted from the mandatory provisions of this Title may come in under the terms and receive the benefits and

be subject to the liabilities of the Title by purchasing workers' compensation insurance or by operating under an approved self insurance program.

§42-1-390 – Withdrawal of waiver of exemption by employer:

> Any employer who, having elected to come in under this Title, being at the time exempt from this Title, and subsequently desiring to withdraw from under its terms, may give notice by cancelling its workers' compensation insurance or self-insurance privileges.

Amending the above Sections would enable the Commission to repeal two corresponding regulations that have been the source of extensive litigation and confusion. The regulations are as follows:

a. Repeal Regulation 67-403 – Election to Adopt the Act

b. Repeal Regulation 67-404 – Withdrawing from the Act.

7. **Problem Area**: The collection powers of the South Carolina Uninsured Employers' Fund indirectly serve as a deterrent to employers that violate the law by being uninsured. Enhancement of the Fund's ability to collect what taxpayers of South Carolina have ultimately paid on behalf of uninsured employers that have violated our law would at the same time enhance overall employer's compliance with the provisions of the South Carolina Workers' Compensation Act.

Possible Solution: Add paragraph two, §42-7-200, that would strengthen the Fund's ability to obtain indemnification for claims that it has paid on behalf of uninsured employers.

What additions to §42-7-200 might look like:

Add paragraph H and I to §42-7-200. Workers' Compensation Uninsured Employer's Fund; claims; collection powers; reimbursement agreements; funding. The paragraph would read as follows:

H. There is a presumption that any employer who is subject to the South Carolina Workers' Compensation Act and is or has been found to be an unqualified self insurer for at least one year has committed an unfair trade practice in violation of §39-5-20. When the South Carolina Workers' Compensation Uninsured Employers' Fund has paid a claim on behalf of an employer who has committed an unfair trade practice as defined above and the employer has neglected to refused to indemnify the Fund, and the unpaid indebtedness owed the Fund has been reduced to a judgment, the South Carolina Workers' Compensation Uninsured Employers' Fund may bring an action under §39-5-140 to recover three times the amount of the unpaid judgment.

I. There is a presumption that an employer who has acted as an unqualified self insurer has violated public policy. When the employer is a corporation, limited liability company, or other such limited liability business entity, and has neglected or refused to repay the workers' compensation Uninsured Employers' Fund for uninsured claims that have been paid on its behalf, and the amount owed the Fund has been reduced to a judgment, the workers' compensation Uninsured Employers' Fund may initiate supplemental proceedings in its collection efforts for the purpose of piercing the limited liability veil. Violation of public policy satisfies a test to determine whether a limited liability veil can be pierced.

8. **Problem Area**: Willfully, uninsured employers. The Commission routinely prosecutes uninsured employers at order and rule to show cause hearing. However, these are civil actions that assess fines and penalties that are often uncollectible, and some employers ignore Commission Orders that assess fines and penalties. There is a section in the Act for criminal

prosecution of willfully uninsured employers (§42-5-45), but the penalties are insufficient to serve as an effective deterrent.

Possible Solutions: Strengthen the provisions of §42-5-45, which presently reads as follows:

> Any employer required to secure payment of compensation under this Title who willfully refuses to secure such compensation shall be guilty of a misdemeanor and upon conviction shall be punished by a fine of not less than $100.00 nor more than $1,000.00 or by imprisonment for not less than thirty days nor more than six months, or both, in the discretion of the court.

What a statutory section might look like: Amend §42-5-45 to read as follows:

> 1. Any employer required to secure payment of compensation under this Title who willfully refuses to secure such compensation shall be guilty of a misdemeanor for the first offense and upon conviction shall be fined not less than $3,000.00 nor more than $5,000.00, or imprisoned for not less than thirty days nor more than six months, or both, in the discretion of the court;
>
> 2. For a second or subsequent conviction, an employer shall be guilty of a felony and shall be fined not less than $5,000.00 or more than $10,000.00, or imprisoned not less than one year nor more than five years, or both, in the discretion of the court.

9. **Problem Area**: Employers that are subject to the Act and uninsured endanger the public safety by operating worksites that are effectively insured by the taxpayers of South Carolina through the South Carolina Uninsured Employers' Fund.

Florida's Division of Workers' Compensation (DWC) has had considerable success in enhancing compliance by using tough enforcement tools lawmakers gave the agency as part of

the 2003 Workers' Compensation Reform. One tool is stop work orders, which DWC uses to bring worksites into compliance.

Possible Solution: Create a statutory mechanism whereby work at uninsured worksites can be identified and stopped.

What a statutory section might look like:

1. Notwithstanding any actions prosecuted or ordered by the SC Workers' Compensation Commission pursuant to §42-5-45, the Commission, in an open hearing with the right of appeal, may find an employer's failure to comply with workers' compensation coverage requirements under this Title poses an immediate danger to public health, safety, and welfare, and authorize a stop-work order to be enforced by the Commission.

2. The Commission may issue a stop-work order within 72 hours of a finding. The order shall take effect when served upon the employer or, for a particular employer worksite, when served upon an appropriate person as that worksite. In addition to serving a stop-work order at a particular worksite, which shall be effective immediately, the Commission shall immediately proceed with service upon the employer which shall be effective upon all employer worksites in the state for which the employer is not in compliance. A stop-work order may be served with regard to an employer's worksite by posting a copy of the stop-work order in a conspicuous location at the worksite. The order shall remain in effect until the Commission issues an order releasing the stop-work order upon a finding that the employer has come into compliance with the coverage requirements of this chapter and paid any penalty assessed under this Title. The Commission may issue an order of conditional release from a stop-work order to an employer upon a finding that the employer has complied with coverage requirements of

this chapter and has agreed to remit periodic payments of the penalty pursuant to a payment agreement schedule with the Commission. If an order of conditional release is issued, failure by the employer to meet any term or condition of such penalty payment agreement shall result in the immediate reinstatement of the stop-work order, and the entire unpaid balance of the penalty shall become immediately due. Commission may require an employer who is found to have failed to comply with the coverage requirements under this Title to file with the Commission, as a condition of release from a stop-work order, periodic reports for a probationary period that shall not exceed 2 years that demonstrates the employer's continued compliance with this Title. The Commission shall by properly promulgated regulation specify the reports required and the time for filing.

3. Stop-work orders and penalty assessment orders issued under this section against a corporation, limited liability company, partnership, or sole proprietorship shall be in effect against any successor business entity including one or more of the same principals against which the stop-work order was issued and who are engaged in the same or equivalent trade or activity.

4. The Commission shall assess an interim daily penalty of $1,000 against one or more principals within the offending uninsured employer for each day the employer conducts business operations in violation of a stop-work order. The interim penalty shall be reduced to an order of the Commission at the conclusion of the stop-work action, which shall be perfected as a civil judgment. Concurrent with an interim penalty, the Commission may file a complaint in the circuit court to restrain any employer who has failed to obey the stop-work order. Any law enforcement agency in the state may, at the

request of the Commission, render any assistance necessary to carry out the provisions of a stop work order, including, but not limited to, preventing any employee or other person from remaining at a place of employment or jobsite after a stop-work order or injection has taken effect.

10. **Problem Area**: Employers often complain they lose bids because their competitors are uninsured, deliberately hiding payroll from assessment, or misclassifying employees; therefore, the cost of workers' compensation insurance is not fairly factored into the bid. It is patently unfair for citizens who want to obey the law are treated unfairly because the economic playing field is not level.

Possible Solution: Provide a civil cause of action to contractors who lose a bid because a competitive bid did not include the cost or accurate cost of workers' compensation insurance.

What a statutory section might look like:

1. Any person, employer or business entity, who loses a competitive bid for a contract shall have a cause of action for damages against the person awarded the contract for which the bid was made, if the person making the losing bid establishes that the winning bidder knew or should have known that he or she was subject to the provision of Title 42 and acting as an unqualified self-insurer while performing the work under the contract, or was insured but had paid a lower rate for insurance by hiding payroll from premium assessment or misclassifying employees.

2. To recover in an action brought under this section, a party must establish a violation by a preponderance of the evidence.

3. Upon establishing that the winning bidder knew or should have known of the violation, the person shall recover as liquidated damages either, whichever is greater, 30

percent of the total amount bid on the contract by the person bringing the action, or $30,000, whichever is greater.

4. In any action under this section, the prevailing party is entitled to an award of reasonable attorney's fees.

5. An action under this section must be commenced within 2 years after the performance of all activities under the contract.

6. A person may not recover any amounts under this section if the defendant in the action establishes by a preponderance of the evidence that the plaintiff:

(a) Was subject to the provision of Title 42 and acting as an unqualified self-insurer at the time of making the bid on the contract, or was insured but had paid a lower rate for insurance by hiding payroll from premium assessment or misclassifying employees;

(b) Was subject to provision of Title 42-1-360 and acting as an unqualified self-insurer with respect to any contract performed by the plaintiff within 1 year before making the bid on the contract.

(c) Any person who loses a competitive bid may petition the court to join in a suit brought under this section by another person against the winning bidder on the same contract and shall be joined in such suit, if more than one person is joined against the winning bidder and such persons prevail in the suit, the court must enter judgment dividing damages recoverable under this section between the parties equally.

(d) Any person who receives notice by publication of a suit filed under this section and fails, within 90 days after receipt of such notice, to petition the court

to join as a party to the suit is barred from bringing a cause of action under this section against the winning bidder on the contract at issue.

11. **Problem area**: Building projects are often uninsured, and the means of detecting them is presently nonexistent. Essentially, the taxpayers of South Carolina are responsible for paying compensable claims that arise out of uninsured building projects.

Possible Solution: Add a section to the Act that requires proof of workers' compensation insurance before a building permit is issued.

What a statutory section might look like:

Every contractor of builder shall, as a condition for applying for and receiving a building permit in South Carolina, arising out of a for-profit construction activity, show proof and certify to the permit issuer that it has secured compensation of employees on the jobsite under this Title. Such proof of compensation must be evidenced by a certificate of coverage issued by an agent, carrier, or authorized self-insurer.

12. **Problem Area**: Premium audits disputes are presently a matter in which the SC Workers' Compensation Commission does not get involved. The SC Department of Insurance hears some cases involving disputed classification codes, but does not hear cases involving audit disputes that have arisen out of purported statutory employer or independent contractor arrangements. This causes a great deal of confusion in the marketplace because disputes, when they are not first heard by an administrative agency, can only be resolved by a declaratory action of a civil court, which is incredibly time-consuming and heard by non-insurance experts. South Carolina is badly in need of a defined simple and rapid audit dispute resolution process. Audit disputes are costly for both employers and carriers, particularly since resolution occurs in an undefined litigation wilderness. The costs are ultimately passed on to consumers.

Possible Solution: Add a section to the Act that creates a mechanism whereby premium audit disputes can be resolved in a timely fashion.

What a statutory section might look like:

1. Employers shall make available all records necessary for the carrier or self-insurer's payroll verification audit and permit the auditor to make a physical inspection of the employer's operation. If the employer fails upon request of the auditor to provide access to the documents specified and the carrier cannot complete the audit as a result, the employer shall pay $5,000 to the carrier to defray the costs of the audit. The penalty may be enforced by judgment in the civil courts of this state.

2. If an employer understates or conceals payroll, or misrepresents or conceals employee duties so as to avoid proper classification for premium calculations, or misrepresents or conceals information pertinent to the computation and application of an experience rating modification factor, the employer shall pay to the insurance carrier a penalty 10 times the amount of the difference in premium paid and the amount the employer should have paid and reasonable attorney's fees. The penalty may be enforced by judgment in the civil courts of this state.

3. If an employer fails to provide reasonable access to payroll records for a payroll verification audit, the employer shall pay a premium to the carrier or self-insurer not to exceed three times the most recent estimated annual premium. The penalty may be enforced by judgment in the civil courts of this state.

4. Carriers are entitled to assess premium on the basis of the total payroll paid or payable by the insured for services of individuals who could realistically receive workers' compensation benefits for work-related injuries as provided by the policy.

Assessment of additional premium by audit is based on whether a reasonable person would conclude that a claimant could potentially receive workers' compensation benefits under a policy.

5. Employers that have been audited and assessed additional premium have the right of appeal. The audit appeal process for all premium audit disputes is 1) the insurance carrier; 2) the state rating and classification bureau in effect at the time of the audit; 3) the South Carolina Workers' Compensation Commission; 4) the court of appeals.

6. In the event an employer is unable to resolve a dispute with the insurance carrier and appeals to the state rating and classification bureau, the bureau will make a determination whether the appeal involves a technical matter related to a rating issue or classification code or an interpretation of state law. If the former, the bureau is authorized to issue an appealable technical finding; if the latter, the bureau will notify the party that the SC Workers' Compensation Commission is the proper agency for filing an appeal.

7. A premium audit appeal may be heard by a Commissioner of the SC Workers' Compensation Commission; however, the Commission is authorized to deputize administrative hearing officers to resolve disputes. A hearing officer so deputized is not required to be an employee of the Commission.

8. The Commission is authorized to establish rules and procedures to be followed at audit disputes. Absent a motion by a party for a hearing, or requirement by a hearing officer of a hearing for fact-finding purposes, a hearing officer is authorized to issue findings without a hearing, after examination of evidence that has been submitted by the employer and insurance carrier, or evidence obtained by the Commission. At a hearing,

the hearing officer is authorized to take sworn testimony and enter evidence into the official record.

9. The Commission may establish reasonable charges to offset costs that arise out of premium audit appeals.

13. **Problem Area**: Cash payment and misclassification schemes are epidemic in South Carolina, and the underlying hidden costs are passed on to consumers in the form of increased rates.

Possible South Carolina solution: Add a section to the Act that upgrades compliance of employers and carriers regarding miscounting or misclassifying of employees, or violating rules or regulations that govern how employees are to be counted and classified.

What a statutory change might look like:

1. Notwithstanding inherent investigative authority or prosecution by the Attorney General regarding false statements or misrepresentation, as defined by **§38-55-530** or other applicable sections, the SC Workers' Compensation Commission is authorized to investigate allegations or suspicions of a false report of business activities, miscount or misclassification by an employer of its employees and/or an undeserved economic benefit that arise out of violation of rules or regulations that govern policies of workers' compensation insurance issued in this state. Nothing in this section precludes other agencies that have jurisdiction over insurance or related criminal matters from conducting their own investigations, and reporting violation of criminal conduct as per the requirements of **§38-55-570** or other applicable sections.

2. In the event of an investigation undertaken by the Commission, the Commission may subpoena an employer or its agents and require the production of any documents or

records which the Commission considers relevant to its investigation. The subpoena shall be returnable at the office designated by the Commission. In the case of refusal to obey a subpoena issued to any person or agent of any employer, a court of common pleas upon application of the Commission, may issue an order requiring the person or agent of an employer to appear at the designated place and produce documentary evidence or give evidence concerning the matter under inquiry.

3. The Commission is authorized to participate in inter-agency task forces for the purposes of investigating and prosecuting premium fraud, which includes but is not limited to so-called under-the-table payroll and/or check cashing schemes.

14. **Problem Area:** Out-of-state employers that come into South Carolina are often insured in other states, but whether coverage extends to South Carolina depends on language in individual policies. This often creates litigation nightmares before the Commission, and decisions are frequently appealed.

Possible solution: Add a section to the Act that enhances compliance of out-of-state employers that operate in South Carolina.

What a statutory section might look like:

1. Employers subject to this Title that have employees engaged in work in this state shall obtain a South Carolina policy or endorsement for such employees that utilizes South Carolina class codes, rates, rules and manuals that are in compliance with and approved under this chapter and the South Carolina Insurance Code. Failure to comply with this paragraph constitutes an undeserved economic benefit or advantage. This is a misdemeanor offense punishable by no more than one year imprisonment or no more

than the maximum fine that is authorized to be imposed by a magistrate or like court at the time of the offense, or both.

2. Employees of non-construction industry employers who have their headquarters outside of South Carolina and also operate in South Carolina and who are routinely crossing state lines, but usually return to their homes each night, the employee shall be assigned to the headquarters' state for premium assessment purposes. However, the construction industry employees performing new construction or alterations in South Carolina shall be assigned to South Carolina even if the employees return to their home state each night.

3. The payroll of executive supervisor who may visit a South Carolina location but who are not in direct charge of a South Carolina location shall be assigned to the state in which the headquarters is located.

4. For construction contractors who maintain a permanent staff of employees and superintendents, if any of these employees or superintendents are assigned to a job located in South Carolina, either for the duration of the job or any portion thereof, their payroll shall be assigned to South Carolina rather than the headquarters' state.

5. Employees who are hired for a specific project in South Carolina shall be assigned to South Carolina.

6. Noncompliance shall be cause for the SC Workers' Compensation Commission to facilitate a stop-work order to remain in effect until compliance is demonstrated. In addition, the Commission may facilitate filing criminal charges against a violator before a magistrate or like court.

15. **Problem area**: Tremendous expenditures for public works projects are presently ongoing throughout the United States, to include South Carolina. Many of these public works projects will not be properly insured, which creates hidden costs to consumers in the form of increased rates.

Possible solution: Add a section to the Act that will enhance insurance compliance on South Carolina public works projects by prequalification.

What a statutory section might look like:

1. Publicly-funded employers engaged in public works greater than $250,000 shall be the direct employer of at least 50% of their payroll. In addition, as part of the bidding process, employer/bidders shall submit a Safety Profile that will count at least 30% toward an overall employer's prequalification score. At a minimum, the Safety Profile must include copies of the bidders Experience Rating Worksheet of the prior five years. The worksheets must list the employer's payroll by class code by policy years. The profile must also include copies of the employer's OSHA logs. If the employer/bidder intends to use subcontractors to fulfill the contract, the Experience Rating Worksheets and OSHA logs of such subcontractors must also be submitted. A maximum score for a safety profile shall be calculated by a set number of points, with the final score determined by deducting points.

2. Cash payments are prohibited by publicly-funded employers. This includes all subcontractors within the work chain of a principal publicly-funded employer. A paystub shall be issued, and copies retained for inspection or audit, showing all deduction.

3. During the time period an employer is receiving public funds, the employer must submit copies of its policy declaration pages as part of any compliance review, and the

policy declaration pages of any subcontractor, to demonstrate their payroll and workers classification codes to the insurance companies that are providing workers' compensation insurance. Compliance officers of the SC Workers' Compensation Commission are authorized to examine these documents to verify that the employer is paying sufficient premium.

4. Compliance officers for the SC Workers' Compensation Commission shall also have the authority to review the insurance policies, experience rating worksheets, OSHA logs and payroll records of a contractor and subcontractors and certify that the correct payroll and classification codes have been disclosed to the workers' compensation insurance company. Noncompliance shall be a cause for the Commission to facilitate a stop-work order to remain in effect until compliance is demonstrated. This is not to preclude other agencies that have regulatory oversight over publicly-funded employers from conducting investigations, assessing penalties and fines, or recommending prosecutions for criminal conduct.

16. **Problem area**: Higher tier contractors often have their employees in the construction industry purchase minimum premium "ghost" policies for $750.00. By an employee's purchase of a ghost policy, the employee is in effect saying he is an independent contractor, not an employee, and he is electing not to cover himself under his policy, which he can appropriately do if he is truly an independent contractor, sole proprietor, or partner. However, ghost policies often create more problems than they solve, particularly if an employee that has a ghost policy is injured or if an auditor assesses additional premium on a higher tier contractor at audit time, because an employee gave him a ghost policy, and the auditor opines that the employer he is

working for could be held liable for a workers' compensation claim should the employee with the ghost policy be injured.

Also, fraud is perpetrated frequently in South Carolina by contractors who get an illegal alien that has a driver's license to obtain a ghost policy and the ghost policyholder pays other illegal alien employees in cash. At audit time, the contractor produces the certificate of insurance correlating to the ghost policy.

Possible solution: Some states require that independent contractors, sole proprietors, partners, and members of limited liability companies in the construction industry apply for an independent contractor exemption, which can be presented to a higher tier contractor in lieu of a workers' compensation certificate.

Independent contractor exemptions in the construction industry are not the complete answer to a problem of construction employees obtaining ghost policies, but it creates an additional hurdle that must be crossed, which serves to weed out a number of experience, problematic coverage and compliance situations.

Creating a unit that the South Carolina Workers' Compensation Commission that issues certificate of exemption, such as Florida and Montana have done, would eliminate the simple step that is available now in South Carolina of an employee purchasing a ghost policy from an agent, without having to provide the agent any additional documentation. Lower level construction industry fraud would be mitigated by creating a "bright line" that worker has to cross before he can be classified as an independent contractor.

Application fees could fund an independent contractor verification unit at the South Carolina Workers' Compensation Commission. Also, data could be collected which would enable the Commission to maintain additional information regarding construction industry independent

contractors, sole proprietors, partners, and members of limited liability companies that operate in South Carolina.

What a statutory section might look like:

1. There is created at the South Carolina Workers' Compensation Commission an independent contractor verification unit that processes application for exemptions from the South Carolina Workers' Compensation Act for construction industry independent contractors, sole proprietors, partners, and members of limited liability companies. A certificate of exemption must be requested bi-annually. The unit is to be self-funded from application fees.

2. A person who meets the requirement of this section and receives an independent contractor exemption is not an employee for the purposes of the South Carolina Workers' Compensation Act, nor is he required to cover himself under a personal workers' compensation insurance policy if he has employees. For the purposes of this section, "person" means: a) a sole proprietor; b) a working member of a partnership; c) a working member of a limited liability company.

3. The Commission shall adopt rules relating to an original application for or renewal of an independent contractor exemption certificate. The Commission shall adopt by rule the amount of the fee for an application or certificate renewal. The application or renewal must be accompanied by the fee.

4. To obtain an independent contractor exemption certificate, the applicant shall swear to and acknowledge the following:

(a) That the applicant has been and will continue to be free from control or direction over the performance of the person's own services, both under contract and in fact;

(b) That the applicant is engaged in an independently established trade, occupation, profession or business and will provide sufficient documentation of that fact to the Commission;

(c) An applicant for an independent contractor exemption certificate shall submit an application under oath on a form prescribed by the Commission and containing the following:

i) the applicant's name and address;

ii) the applicant's Social Security number, which is subject to verification by the Commission;

iii) each occupation for which the applicant is seeking independent contractor certification;

iv) and other documents as provided by Commission rule to assist in determining if the applicant has an independently established business.

5. The Commission shall issue an independent contractor exemption certificate to an applicant if the Commission determines that an applicant meets the requirements of this section.

6. When the Commission approves an application for an independent contractor exemption certificate and the person is working under the independent contractor exemption certificate, the person's status is conclusively presumed to be that of an independent contractor.

7. A person working under an approved independent contractor exemption certificate has waived all rights and benefits under the South Carolina Workers' Compensation Act and is precluded from obtaining benefits from a statutory employer.

8. Once issued, an independent contractor exemption certificate remains in effect for 2 years unless:

(a) suspended or revoked pursuant to rules adopted by the Commission pursuant to this section;

(b) canceled by the independent contractor;

(c) If the Commission denies an application for an independent contractor exemption certificate, the applicant may contest that decision as provided by rules adopted by the Commission pursuant to this section.

9. An independent contractor in the construction industry may elect to cover himself under a policy at any time an exemption is in effect. However, a policy does not cancel the exemption, but only supersedes the exemption for the specific period coverage is in place. If the policy is cancelled, the independent contractor exemption governs.